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MICHAEL RODAK, JR., CLERK

In the Supreme Court of the United States

OCTOBER TERM, 1973

73-781

FRITZ SCHERK,

Petitioner,

vs.

ALBERTO-CULVER COMPANY,

Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

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FRITZ SCHERK,

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PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

Fritz Scherk hereby petitions that a writ of certiorari issue to review the judgment and opinion of the United States Court of Appeals for the Seventh Circuit entered on August 2, 1973.

OPINIONS BELOW

The majority and dissenting opinions of the United States Court of Appeals for the Seventh Circuit are not yet officially reported. The opinions are unofficially reported, [Current Binder] CCH Fed. Sec. L. Rep. ¶ 94,092, and are printed in the Appendix at pages App. 1-App. 17. The opnion of the United States District Court for the

Northern District of Illinois, Eastern Division, is not reported either officially or unofficially and is printed in the Appendix at pages App. 18-App. 33.

JURISDICTION

The Seventh Circuit's judgment was entered on August 2, 1973. (App. 34.) Petitioner's timely petition for rehearing was denied on October 18, 1973. (App. 35.) The jurisdiction of this Court is invoked under 28 U.S.C. §1254(1).

QUESTION PRESENTED

Whether unambiguous contractual provisions requiring arbitration of an international commercial dispute, which provisions were the result of arms-length bargaining by sophisticated businessmen and lawyers, are unenforceable merely because a claim, as yet not proven, has now been made that the Securities Exchange Act of 1934 has been violated.

STATUTES INVOLVED

The statutes involved herein are the Federal Arbitration Act, 9 U.S.C. §§2, 3, 201, 202, 206, and 208, and the Securities Exchange Act of 1934, 15 U.S.C. §78cc(a). The text of these provisions are reproduced in the Appendix at pages App. 36-App. 38.

STATEMENT OF THE CASE

Respondent Alberto-Culver Company brought this action charging that Mr. Scherk breached certain contract warranties and violated Section 10(b) of the Securities Exchange Act of 1934 (the "Exchange Act"), 15 U.S.C. §78j (b), Rule 10b-5 promulgated pursuant thereto, and common law. Jurisdiction of the District Court was predicated upon Section 27 of the Exchange Act, 15 U.S.C. §78aa, and 28 U.S.C. § 1332.

Alberto-Culver is a Delaware corporation which manufactures and distributes toiletries and hair products in national and international markets. Mr. Scherk is a German citizen, residing in Switzerland, who, prior to the dealings with Albert-Culver was in the business of manufacturing and selling cosmetics in Europe. Mr. Scherk owned three businesses: Firma Ludwig Scherk ("FLS"), a German sole proprietorship which manufactured cosmetics; Scherk Establissement Vaduz ("SEV"), a Liechtenstein business entity with no counterpart in the United States, which licensed trademarks for cosmetics on an international basis; and Lodeva Herstellung und Vertrieb kosmetischer Artikel Gmbh ("Lodeva"), a dormant German business entity with no counterpart in the United States.

Interested in gaining an entree into the European market, Alberto-Culver contacted Mr. Scherk in Germany in June of 1967 to explore a possible acquisition of his European cosmetic business. Protracted negotiations ensued, resulting in Alberto-Culver's acquisition of FLS, SEV and Lodeva. Alberto-Culver conducted an exhaustive examination of the businesses, including an audit by Peat, Marwick, Mitchell & Co. The closing took place in June, 1969. Alberto-Culver acquired the assets of FLS and all of Scherk's interest in Lodeva. As to SEV, Alberto-Culver specified which assets it was buying, but for tax purposes required that the acquisition take place as a sale of stock. Therefore, SEV was transformed into a stock company by Alberto-Culver's attorneys acting as escrow agents. Alberto-Culver paid Scherk cash and delivered four promissory notes. The one negotiable note may not be negotiated without prior approval by Alberto-Culver and is restricted as to whom it may be sold or transferred. (Mr. Scherk has found that

he cannot sell that note to any Swiss banks.) The other three notes are by their terms non-negotiable and must be surrendered to Alberto-Culver.

In the FLS and SEV contracts, Alberto-Culver and Mr. Scherk specifically agreed that any and all disputes arising concerning the transactions were to be arbitrated before the International Chamber of Commerce ("ICC") in Paris, France.* In 1970, Alberto-Culver concluded that Mr.

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* The FLS contract provides:

"The parties agree that if any controversy or claim shall arise out of this agreement or the breach thereof, the matter shall be settled exclusively by arbitration in accordance with the rules then obtaining of the International Chamber of Commerce, Paris, France, by a single arbitrator, if the parties shall agree upon one, or by one arbitrator appointed by each party and a third arbitrator appointed by the other arbitrators. In case of any failure of a party to make an appointment referred to above within four (4) weeks after notice of the controversy, such appointment shall be made by said Chamber. Unless otherwise agreed, all arbitration proceedings shall be held in Paris, France, and each party agrees to comply in all respects with any award made in any such proceeding and to the entry of a judgment in any jurisdiction upon any award rendered in such proceeding. The laws of the State of Illinois, U.S.A. shall apply to and govern this agreement, its interpretation and performance."

The SEV contract provides:

"The parties agree that if any controversy or claim shall arise out of this agreement or the breach thereof and either party shall request that the matter shall be settled by arbitration, the matter shall be settled exclusively by arbitration in accordance with the rules then obtaining of the International Chamber of Commerce, Paris, France by a single arbitrator, if the parties shall agree upon one, or by one arbitrator appointed by

Scherk had breached his contractual warranties as to the trademarks owned by FLS and SEV. Instead of instituting arbitration as required by the contracts, Alberto-Culver brought suit in the United States District Court in Chicago. Mr. Scherk moved in the District Court, pursuant to 9 U.S.C. §3, for an order staying these proceedings pending arbitration, and he instituted arbitration before the ICC in Paris. The District Court denied the requested stay and enjoined Mr. Scherk from proceeding with arbitration before the ICC. Mr. Scherk appealed both of these orders. The Seventh Circuit panel hearing the case affirmed, Judge Stevens dissenting.

(footnote continued)

each party and a third arbitrator appointed by the other arbitrators. In case of any failure of a party to make an appointment referred to above within four weeks after notice of the controversy, such appointment shall be made by said Chamber. All arbitration proceedings shall be held in Paris, France, and each party agrees to comply in all respects with any award made in any such proceeding and to the entry of a judgment in any jurisdiction upon any award rendered in such proceeding. The law of the State of Illinois, U.S.A. shall apply to and govern this agreement, its interpretation and performance."

REASONS FOR GRANTING THE WRIT

This is an important case of first impression. The Seventh Circuit has concluded that the mere filing of a claim that the Exchange Act has been violated is sufficient to nullify explicit contractual provisions requiring arbitration of an international commercial dispute. The Seventh Circuit's decision is in flat contradiction to declared Congressional policy, 9 U.S.C. §201 *et seq.*, and principles concerning international commercial transactions recently enunciated by this Court in *M. S. Bremen* v. *Zapata Off-Shore Co.*, 407 U.S. 1 (1972). Given the almost limitless expanse of commercial conduct now being covered by federal securities law, this opinion will have widespread, detrimental and wholly unexpected effects on international commerce. Thus, this case involves an issue of exceptional importance meriting review by this Court.

A. The Decision Below Effectively Nullifies Chapter Two Of The Federal Arbitration Act.

In 1970, having considered the appropriateness of, and the benefits to be gained from, arbitration in the international context, Congress enacted Chapter 2 of the Federal Arbitration Act. 9 U.S.C. §201 *et seq.* Chapter 2 provides that an international commercial contract providing for arbitration is enforceable and irrevocable. 9 U.S.C. §§202, 208. The courts of the United States are to compel such arbitration proceedings. 9 U.S.C. §§206, 208. The panel majority in the decision below completely ignored the applicable and controlling provisions of the Federal Arbitration Act and the declared national policy contained therein. In effect, the panel's decision nullifies the Federal Arbitration Act vis-a-vis a vast number of international commercial transactions.

B. The Decision Below Conflicts With This Court's Recent Decision Regarding International Commercial Transactions.

The panel majority's decision conflicts with the controlling policy considerations enunciated by this Court in *M. S. Bremen* v. *Zapata Off-Shore Co.*, 407 U.S. 1 (1972).

In *Zapata,* this Court determined that, in *international* commercial matters, agreements as to choice of forum are valid and will be enforced. This is so even if the foreign tribunal will enforce contractual, exculpatory clauses which are contrary to the domestic policy of this country. This Court concluded that forum-selection clauses

> "are prima facie valid and should be enforced unless enforcement is shown by the resisting party to be 'unreasonable' under the circumstances." (Footnote omitted.) 407 U.S. at 10.

This, the Court noted, is particularly so when, as in the instant case, the agreement is the result of arm's-length bargaining by sophisticated businessmen. 407 U.S. at 12. In the case at bar, there has been absolutely no showing that enforcement of the arbitration provisions would be in any way unreasonable. The policy considerations relating to international commerce which dictated enforcement of the forum selection clause in *Zapata* apply with equal force to the issue of enforcing the arbitration clauses in the case at bar.

C. The Wilko Decision Should Be Re-Examined In Light Of The Requirements Of International Commerce.

The only authority for the position of the panel majority is *Wilko* v. *Swan,* 346 U.S. 427 (1953), wherein this Court was interpreting §14 of the Securities Act of 1933, 15 U.S.C.

§77n. *Wilko* decided that, in controversies under the Securities Act, agreements to arbitrate future disputes are unenforceable. Since the language of §29(a) of the Exchange Act, 15 U.S.C. §78cc(a), is similar to that of §14 of the Securities Act, courts have applied *Wilko* to Exchange Act cases.

As Judge Stevens notes in his dissenting opinion (App. 15), the *Wilko* result is not required by the express language of §14; instead, this Court was actually extending the ambit of §14. Moreover, *Wilko* was decided solely in a domestic context without any consideration of the requirements of international commerce. Since that 1953 decision, Congress enacted Chapter 2 of the Federal Arbitration Act and this Court decided the *Zapata* case. Judge Stevens stated in his dissenting opinion:

> "... I consider it plain that the policy of the 1934 Act would not be thwarted by enforcing this agreement, whereas the strong countervailing policy identified by the Chief Justice in *Zapata* will be compromised if it is not enforced." (App. 16, n.13.)

Furthermore, the *Wilko* result was largely influenced by the fact that the parties there were of quite different bargaining strength, that is, purchasers of securities dealing with brokerage houses. See 346 U.S. at 435. Here, the arbitration agreement was reached through arm's-length bargaining between sophisticated businessmen. As Judge Stevens said (App. 17):

> "[t]he dispute between these parties over the alleged shortage in defendant's inventory of European trademarks, a matter covered by contract warranties and subject to pre-closing verification, is the kind of commercial dispute for which arbitration is entirely appropriate."

D. This Case Should Be Reviewed By This Court Because The Seventh Circuit's Decision, If Left Standing, Will Have Wide-Ranging, Unexpected, Indeed Detrimental Effects Upon International Commercial Transactions.

The effect of Seventh Circuit's decision is that, in international commercial transactions as long as securities are involved in some way, the parties cannot rationally decide in advance to arbitrate future disputes. Thus, the parties are forbidden to add this element of certainty and specificity to their transactions and are precluded from choosing in advance to resolve their disputes inexpensively and expeditiously by arbitration, rather than litigation.

The broad sweep of this decision can only be appreciated by an understanding of the vast scope of the definition of "security." Section 3(a)(10) of the Exchange Act, 15 U.S.C. §78c(a)(10), defines security as:

> "any note, stock, treasury stock, bond, debenture, certificate of interest or participation in any profit-sharing agreement or in any oil, gas, or other mineral royalty or lease, any collateral-trust certificate, preorganization certificate or subscription, transferable share, investment contract, voting-trust certificate, certificate of deposit, for a security, or in general, any instrument commonly known as a 'security'; or any certificate of interest or participation in, temporary or interim certificate for, receipt for, or warrant or right to subscribe to or purchase, any of the foregoing; but shall not include currency or any note, draft, bill of exchange, or banker's acceptance which has a maturity at the time of issuance of not exceeding nine months, exclusive of days of grace, or any renewal thereof the maturity of which is likewise limited."

Thus, securities in some form are present in a great variety and a vast number of international commercial transactions.

As this Court stated in *Zapata*:

> "[f]or at least two decades we have witnessed an expansion of overseas commercial activities by business enterprises based in the United States. The barrier of distance that once tended to confine a business concern to a modest territory no longer does so. . . . The expansion of American business and industry will hardly be encouraged if, notwithstanding solemn contracts, we insist on a parochial concept that all disputes must be resolved under our laws and in our courts. . . . *We cannot have trade and commerce in world markets and international waters exclusively on our terms, governed by our laws, and resolved in our courts.*" (Emphasis added.) 407 U.S. at 8-9.

As Judge Stevens noted (App. 10):

> "[a]n excessively paternalistic attitude toward American overseas investment will inevitably make American capital less attractive to foreign firms."

This Court has recognized that, in international commercial dealings, the method of and forum for, handling possible future disputes is a proper subject of bargaining, a term which is likely to effect the price of the transaction, and, more importantly, a term without which there may be no transaction at all. This Court stated:

> "[t]he elimination of all such uncertainties by agreeing in advance on a forum acceptable to both parties is an *indispensable element* in international trade, commerce and contracting." (Emphasis added.) 407 U.S. at 13-14.

Not only will the effects of the panel's decision hinder development of American overseas trade and commerce, it adversely affects the credibility of American business. In plain English, Alberto-Culver agreed to arbitrate in Paris before the ICC. Now after the fact, while it is suing Mr. Scherk on the very contracts in issue, Alberto-Culver says that it has an absolute right to renege on its commitments. This Court should consider whether our judicial system is going to let sophisticated American businesses go abroad, make solemn contracts with foreigners and then renege on their commitments.

CONCLUSION

For the foregoing reasons, it is respectfully submitted that this Court should grant the Petition for a Writ of Certiorari to review the decision of the Court of Appeals for the Seventh Circuit.

Respectfully submitted,

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PROOF OF SERVICE

ROBERT F. HANLEY, on oath deposes and states that on the 14th day of November, 1973, three copies of the Petition for a Writ of Certiorari were served by first class mail, postage prepaid, on Francis J. Higgins, at 135 South LaSalle Street, Chicago, Illinois 60603, and that all parties required to be served have been served.

/s/ ROBERT F. HANLEY
One IBM Plaza
Chicago, Illinois 60611
Attorney for Petitioner

Subscribed and sworn to
before me this 14th day
of November, 1973.

.....
Notary Public

APPENDIX A

In the

United States Court of Appeals

For the Seventh Circuit

No. 72-1158

ALBERTO-CULVER COMPANY, a Delaware corporation,
Plaintiff-Appellee,

vs.

FRITZ SCHERK,
Defendant-Appellant.

Appeal from the United States District Court for the Northern District of Illinois, Eastern Division.

OPINION

August 2, 1973

Before STEVENS, *Circuit Judge,* GRANT, *Senior District Judge,* and GORDON, *District Judge.*

GORDON, *District Judge.* This is an interlocutory appeal. The district court found that it had jurisdiction over both the parties and the subject matter of this lawsuit. Also, the district court refused to stay the proceedings before it while the parties arbitrated their dispute before the International Chamber of Commerce tribunal in Paris,

France. The court enjoined the parties from such arbitration.

The appellee urges that the findings and order of the district court are not appealable under 28 U.S.C. § 1292 (a)(1) and has moved for dismissal of the appeal. For the reasons set forth in this opinion, we find that this court may properly entertain the appeal, and we affirm the decision of the district court.

The plaintiff-appellee, Alberto-Culver (Alberto) is a Delaware corporation with its principal offices situated in Illinois. It manufactures and distributes toiletries and hair products in national and international markets.

The defendant-appellant, Fritz Scherk (Scherk) is a German citizen who presently resides in Switzerland. Prior to the transactions here in issue, Scherk was engaged in the manufacture and sale of cosmetic products for sale in western Europe. The principal manufacturing operations were conducted by Scherk in facilities situated within Berlin, Germany, and owned by Scherk through a sole proprietorship called Firma Ludwig Scherk (FLS).

Scherk also owned interrelated business entities known as Scherk Establissement Vaduz (SEV), a Liechtenstein entity which has no counterpart in the United States, and Lodeva Herstellung und Vertrieb Kosmetischer Artikel GMBH (Lodeva), a German entity which has no counterpart in the United States. SEV was operated by Scherk as a holding company licensing the sale and distribution of Scherk's cosmetics on an international basis under a variety of trademarks. The Lodeva entity was dormant and remains so.

In June, 1967, Alberto contacted Scherk in Germany to explore the possibility that Scherk might sell his

European cosmetic business. In November, 1967, Fred Maeding of Alberto visited Scherk in Germany to pursue negotiations for such acquisition. In December, 1967, Alberto's president, Leonard H. Lavin, met with Scherk's representative, Benjamin Navon, in Chicago, Illinois. The negotiations were terminated.

In February, 1968, Alberto contacted Scherk in Berlin and negotiations were resumed. An agreement in principle was reached at this time concerning the basic terms for Alberto's acquisition of Scherk's business entities, SEV, FLS, and Lodeva; the details of the agreement were hammered out in Melrose Park, Illinois, during a 3-day meeting held in late May and early June, 1968. Scherk was present in Illinois for this latter meeting. A written document was ultimately prepared and signed in Vienna, Austria, by Scherk in February, 1969.

Among other things, the agreement between Alberto and Scherk provided that SEV was to be converted to a stock corporation and that Alberto was to acquire 100% of the stock of the new corporation. Accordingly, the parties entered into an escrow agreement by which Scherk assigned all of his rights in SEV to the escrow agent who was to accomplish the conversion and hold the certificates until closing.

The agreement also provided that as to the acquisition of SEV that:

> "The parties agree that if any controversy or claim shall arise out of this agreement or the breach thereof and either party shall request that the matter shall be settled by arbitration, the matter shall be settled exclusively by arbitration in accordance with the rules then obtaining of the International Chamber of Commerce, Paris, France, by a single arbitrator, if the parties shall agree upon one, or by one arbitrator

appointed by each party and a third arbitrator appointed by the other arbitrators. In case of any failure of a party to make an appointment referred to above within four weeks after notice of the controversy, such appointment shall be made by said Chamber. All arbitration proceedings shall be held in Paris, France, and each party agrees to comply in all respects with any award made in any such proceeding and to the entry of a judgment in any jurisdiction upon any award rendered in such proceeding. The law of the State of Illinois, U.S.A. shall apply to and govern this agreement, its interpretation and performance."

The agreement provided that as to the acquisition of FLS that:

"The parties agree that if any controversy or claim shall arise out of this agreement or the breach thereof, the matter shall be settled exclusively by arbitration in accordance with the rules then obtaining of the International Chamber of Commerce, Paris, France, by a single arbitrator, if the parties shall agree upon one, or by one arbitrator appointed by each party and a third arbitrator appointed by the other arbitrators. In case of any failure of a party to make an appointment referred to above within four (4) weeks after notice of the controversy, such appointment shall be made by said Chamber. Unless otherwise agreed, all arbitration proceedings shall be held in Paris, France, and each party agrees to comply in all respects with any award made in any such proceeding and to the entry of a judgment in any jurisdiction upon any award rendered in such proceeding. The laws of the State of Illinois, U.S.A. shall apply to and govern this agreement, its interpretation and performance."

The closing of the transaction was accomplished in Geneva, Switzerland, in June, 1969. Nearly one year later,

Alberto discovered that the trademark rights purchased from Scherk were subject to substantial encumbrances. A dispute arose, and Alberto attempted to rescind the purchase agreement; it tendered the business to Scherk, who refused to accept the tender.

Scherk first took steps to institute arbitration in early 1971; however, a request for arbitration was not filed with the International Chamber of Commerce until November 9, 1971. Alberto commenced the instant action in the district court for the northern district of Illinois on June 11, 1971, alleging that it was defrauded in the acquisition of these businesses in violation of Section 10(b) and Rule 10b-5 of the Securities Exchange Act of 1934, 15 U.S.C. § 78a et seq.

As pertinent here, 28 U.S.C. § 1292(a) provides:

> "The courts of appeals shall have jurisdiction of appeals from:
>
> (1) Interlocutory orders of the district courts . . . granting, continuing, modifying, refusing or dissolving injunctions. . . ."

The appellee contends that the district court's order preliminarily enjoining Scherk from proceeding with arbitration in Paris and denying a stay of its own proceedings is not an interlocutory injunction within the meaning of 28 U.S.C. § 1292(a)(1). We disagree.

The practical result of the district court's order is to terminate Scherk's recourse to arbitration of the dispute before the International Chamber of Commerce in Paris and as such, the order qualifies as an "injunction" within the meaning of 28 U.S.C. § 1292(a)(1). *Ettleson* v. *Metropolitan Life Insurance Co.*, 317 U.S. 188 (1942); *Shanferoke Co.* v. *Westchester Co.*, 293 U.S. 449 (1935);

Merritt-Chapman & Scott Corp. v. *Pennsylvania Turn. Com'n,* 387 F.2d 768 (3d Cir. 1967); *Cuneo Press* v. *Kokomo Jamdler's Union No. 34,* 235 F.2d 108 (7th Cir. 1956). Accordingly, the motion to dismiss the appeal may not be granted.

The district court based its refusal to stay the proceedings and granted an injunction to bar the parties from proceeding with arbitration before the Paris tribunal on the authority of *Wilko* v. *Swan,* 346 U.S. 427 (1953). That case held that section 14 of the Securities Act of 1933, 15 U.S.C. § 77a et seq., voided agreements made in connection with the purchase of securities to arbitrate disputes which may arise in the future; the aggrieved party has a nonwaivable right to have his dispute determined in a judicial forum. In resolving the conflict between the United States Arbitration Act and the Securities Act of 1933, the Court stated at page 438:

> "Two policies, not easily reconcilable, are involved in this case. Congress has afforded participants in transactions subject to its legislative power an opportunity generally to secure prompt, economical and adequate solution of controversies through arbitration if the parties are willing to accept less certainty of legally correct adjustment. On the other hand, it has enacted the Securities Act to protect the rights of investors and has forbidden a waiver of any of these rights. Recognizing the advantages that prior agreements for arbitration may provide for the solution of commercial controversies, we decided that the intention of Congress concerning the sale of securities is better carried out by holding invalid such an agreement for arbitration of issues arising under the Act."

The appellant seeks to limit the rule of *Wilko* v. *Swan* to domestic transactions and asserts that the correct rule

for international transactions is found in *M. S. Bremen* v. *Zapata Off-Shore Co.*, 407 U.S. 1 (1972). However, the *Bremen* case did not involve the sale of securities and is, therefore, not controlling.

We agree with the district court that the appellant had sufficient contacts within the United States to give the court personal jurisdiction over the appellant. See *McGee* v. *International Life Insurance Co.*, 355 U.S. 220 (1957); *International Shoe Co.* v. *Washington*, 326 U.S. 310 (1945). The question of the district court's jurisdiction turns on whether the transaction here in issue involves "securities" within the purview of Section 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5. We conclude that it does.

Section 3(a)(10) of the Securities Exchange Act of 1934 provides:

> "(10) The term 'security' means any note, stock, treasury stock, bond, debenture, certificate of interest or participation in any profit-sharing agreement or in any oil, gas, or other mineral royalty or lease, any collateral-trust certificate, preorganization certificate or subscription, transferable share, investment contract, voting-trust certificate, certificate of deposit, for a security, or in general, any instrument commonly known as a 'security'; or any certificate of interest or participation in, temporary or interim certificate for, receipt for, or warrant or right to subscribe to or purchase, any of the foregoing; but shall not include currency or any note, draft, bill of exchange, or banker's acceptance which has a maturity at the time of issuance of not exceeding nine months, exclusive of days of grace, or any renewal thereof the maturity of which is likewise limited."

The United States Supreme Court determined in *Tcherepnin* v. *Knight*, 389 U.S. 332 (1969) that this lan-

guage is to be construed broadly to effect the purposes of the act, one of which is "to protect investors through the requirement of full disclosure by issuers of securities". At page 338, the Court stated:

> "As used in the 1933 [Securities Act] and 1934 [Securities Exchange Act] Acts, 'security' embodies a flexible rather than a static principle, one that is capable of adaptation to meet countless and variable schemes devised by those who seek the use of money of others on the promise of profits."

This mandate to construe broadly the term "security" compels our conclusion that the agreement to incorporate the SEV entity, and to transfer the assets of the SEV, FLS and Lodeva entities in exchange for cash and promissory notes involves a "security" within the meaning of the Securities Exchange Act of 1934. *Movielab, Inc.* v. *Berkey Photo, Inc.*, 452 F.2d 662 (2d Cir. 1971); *Lawrence* v. *Securities and Exchange Comm.*, 398 F.2d 276 (1st Cir. 1968).

We find that the district court did not abuse its discretion in refusing to stay the proceedings before it, pending arbitration. The order appealed from is

AFFIRMED.

STEVENS, *Circuit Judge*, dissenting. In the two decades since the Supreme Court considered the collision between the two conflicting policies which made *Wilko* v. *Swan* such a close case,[1] there have been several important develop-

[1] The district court was reversed by a divided court of appeals, *Wilko* v. *Swan*, 201 F.2d 439 (2d Cir. 1953), which was in turn reversed by a divided Supreme Court. See dissenting opinion of Mr. Justice Frankfurter, 346 U.S. at 439, and concurring opinion of Mr. Justice Jackson, *id.* at 438.

ments which significantly affect the wisdom of applying the rule of that case to a transaction such as this. On the other hand, the relevant statutory language has not changed materially and it is not easy to identify a principled basis for distinguishing that case from this. Nevertheless, since I am persuaded that Congress did not intend the Exchange Act of 1934 to hamper the ability of American firms to acquire foreign businesses, I believe this arbitration clause should be enforced.

Since 1953 the policy of encouraging the settlement of disputes by arbitration has received increasingly strong endorsement, see, *e.g.*, *Metro Industrial Painting Corp.* v. *Terminal Construction Co.*, 287 F.2d 382, 385 (2d Cir. 1961); *Prima Paint* v. *Flood & Conklin*, 388 U.S. 395, 404; *Halcon International, Inc.* v. *Monsanto Australia Ltd.*, 446 F.2d 156 (7th Cir. 1971), cert. denied, 404 U.S. 949.[2] During this period overseas commercial activities of American business enterprises have expanded dramatically, adding emphasis to the value of arbitration as a method of adjusting international business disputes.

> "For at least two decades we have witnessed an expansion of overseas commercial activities by business enterprises based in the United States. The barrier of distance that once tended to confine a business concern to a modest territory no longer does so. Here we see an American company with special expertise contracting with a foreign company to tow a complex ma-

[2] Judicial support for arbitration was slow to manifest itself. In an interesting footnote to his opinion in *Kulukundis Shipping Co.* v. *Amtorg Trading Corp.*, 126 F.2d 978 (2d Cir. 1942), Judge Frank reviewed early examples of legislative approval of arbitration to support his comment: "In the light of the clear intention of Congress, it is our obligation to shake off the old judicial hostility to arbitration." *Id.* at 985. See *id.* at 985 n. 24a.

chine thousands of miles across seas and oceans. The expansion of American business and industry will hardly be encouraged if, notwithstanding solemn contracts, we insist on a parochial concept that all disputes must be resolved under our laws and in our courts. Absent a contract forum, the considerations relied on by the Court of Appeals would be persuasive reasons for holding an American forum convenient in the traditional sense, but in an era of expanding world trade and commerce, the absolute aspects of the doctrine of the *Carbon Black* case have little place and would be a heavy hand indeed on the future development of international commercial dealings by Americans. We cannot have trade and commerce in world markets and international waters exclusively on our terms, governed by our laws, and resolved in our courts." *M/S Bremen* v. *Zapata Off-Shore Co.*, 407 U.S. 1, 8-9.[3]

An excessively paternalistic attitude toward American overseas investment will inevitably make American capital less attractive to foreign firms.

At the same time, the coverage of the Exchange Act of 1934 has been growing at a pace which makes it operative in situations quite unlike those in which the Securities Act of 1933 typically applies. The holding in *Wilko* v. *Swan* rested, in part, on the fact that the 1933 Act was intended to give special protection to the relatively uninformed, individual investor.

"While a buyer and seller of securities, under some circumstances, may deal at arm's length on equal

[3] As Judge Gordon points out, the *Zapata* case did not involve the sale of securities and therefore is not controlling here. Moreover, the Chief Justice expressly limited his opinion to international agreements "unaffected by fraud," 407 U.S. at 12. Nevertheless, I believe the policy considerations which underlie that decision are relevant here.

terms, it is clear that the Securities Act was drafted with an eye to the disadvantages under which buyers labor. Issuers of and dealers in securities have better opportunities to investigate and appraise the prospective earnings and business plans affecting securities than buyers. It is therefore reasonable for Congress to put buyers of securities covered by that Act on a different basis from other purchasers.

"When the security buyer, prior to any violation of the Securities Act, waives his right to sue in courts, he gives up more than would a participant in other business transactions. The security buyer has a wider choice of courts and venue. He thus surrenders one of the advantages the Act gives him and surrenders it at a time when he is less able to judge the weight of the handicap the Securities Act places upon his adversary." 346 U.S. 427, 435.[4]

The Exchange Act of 1934 also provides essential protections for the individual investor trading in the imperson-

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[4] The brief for the Securities and Exchange Commission, Amicus Curiae, emphasized the statutory concern for the disadvantaged position of the average investor.

"Congress conceived that securities are 'intricate merchandise', and that the public interest demanded legislation which would recognize the gross inequality of bargaining power between the professionals in the securities business and the average investor." Amicus Brief p. 15.

"The Securities Act of 1933 . . . was designed primarily to protect the less informed members of the public against the professionals, in the light of past experience which indicated that misrepresentations not infrequently were made and that under pre-existing law it was extremely difficult for the customer to obtain adequate redress." *Id.* at 33.

"Contrary to the purpose of Congress, the decision below gives no recognition to the grossly unequal positions of the securities firm and the average customer who, before effecting a purchase, is requested to sign a fine-print form agreement." *Id.* at 45-46.

al securities market. Insofar as that Act proscribes insider trading, "sales against the box" by controlling persons, manipulative and deceptive practices in connection with purchases and sales over a stock exchange, and similar aspects of transactions between the average investor and a relatively more sophisticated broker, dealer, or insider, quite obviously the rationale of *Wilko* v. *Swan* would preclude the enforceability of an agreement to waive a judicial remedy under the Act. For in such situations the same kind of disparity in either information or bargaining power is likely to be present, and there is no more reason to favor arbitration than in disputes arising under the 1933 Act.

But with the application of Rule 10(b)(5) to negotiated transactions in which the amount at stake typically justifies an independent audit or other verification of the property being purchased or sold, and the transfer of securities is a function of the form in which the parties elect to cast their transaction, quite different considerations apply. To the extent that reliance on statutory protection plays a relatively less significant part in the investment decision, there is a correspondingly lesser justification for a prohibition against any waiver of the benefits of the Act. Moreover, in transactions which are sufficiently large and complex that the parties typically contemplate the possibility of future controversy, the method of resolving foreseeable disputes is itself a proper subject of bargaining. In the international market, the inability to agree on a neutral forum quite clearly may have an impact on the price of the transaction, or even the acceptability of a prospective purchaser. The reason for the rule of *Wilko* v. *Swan* simply does not fit this case.

In view of the substantial identity between the language of § 14 of the 1933 Act,[5] and § 29(a) of the 1934 Act,[6] it is not easy to give the two provisions different interpretations. Nevertheless, since even *Wilko* v. *Swan* approves a measure of license in reading § 14,[7] and since even the same words in different parts of the same statute may be read differently,[8] I am persuaded that § 29(a) may be read to permit enforceability of certain agreements to arbitrate disputes which involve a claimed violation of the 1934 Act.

Section 29(a) prohibits the plaintiff from waiving the defendant's compliance with any "provision" of the Act. For present purposes, the relevant "provision" of the 1934 Act is § 27 which authorizes the plaintiff to bring a

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[5] "Any condition, stipulation, or provision binding any person acquiring any security to waive compliance with any provision of this title or of the rules and regulations of the Commission shall be void." 48 Stat. 84, 15 U.S.C. § 77n.

[6] "Any condition, stipulation, or provision binding any person to waive compliance with any provision of this title or of any rule or regulation thereunder, or of any rule of an exchange required thereby shall be void." 48 Stat. 903, 15 U.S.C. § 78cc(a).

[7] The text of § 14 does not support the limitation of the holding to stipulations made before any controversy arose. Moreover, the language prohibiting waiver of "compliance with any provision of this title" could easily have been read to relate to substantive provisions of the Act without including the remedy provisions.

[8] See, *e.g.*, *Puerto Rico* v. *Shell Co.*, 302 U.S. 253, 258-259; *Helvering* v. *Stockholms Enskilda Bank*, 293 U.S. 84, 87-88; *Atlantic Cleaners & Dyers, Inc.* v. *United States*, 286 U.S. 427, 433; *Grand Lodge* v. *King*, 335 F.2d 340, 344-345 (9th Cir. 1964).

civil action in the federal district court.[9] There is no language in the Act obligating the defendant to act in "compliance with" § 27. What is waived—if the arbitration agreement is enforced—is plaintiff's right to sue rather than defendants' obligation to comply with the Act. Thus, enforcement of the arbitration agreement is consistent with a literal reading of the text of §§27 and 29(a).

It is not, however, entirely consistent with the reading given § 14 of the 1933 Act by the Supreme Court in *Wilko* v. *Swan*. But that reading depended less on the

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[9] Section 27 provides:

"Sec. 27. The district courts of the United States, the Supreme Court of the District of Columbia, and the United States courts of any Territory or other place subject to the jurisdiction of the United States shall have exclusive jurisdiction of violations of this title or the rules and regulations thereunder, and of all suits in equity and actions at law brought to enforce any liability or duty created by this title or the rules and regulations thereunder. Any criminal proceeding may be brought in the district wherein any act or transaction constituting the violation occurred. Any suit or action to enforce any liability or duty created by this title or rules and regulations thereunder, or to enjoin any violation of such title or rules and regulations, may be brought in any such district or in the district wherein the defendant is found or is an inhabitant or transacts business, and process in such cases may be served in any other district of which the defendant is an inhabitant or wherever the defendant may be found. Judgments and decrees so rendered shall be subject to review as provided in sections 128 and 240 of the Judicial Code, as amended (U.S.C., title 28, secs. 225 and 347). No costs shall be assessed for or against the Commission in any proceeding under this title brought by or against it in the Supreme Court or such other courts." 48 Stat. 902-903, 15 U.S.C. § 78aa.

text of the statute than on its underlying policy.[10] The text of the 1933 Act, like the text of the 1934 Act, renders void any waiver by a plaintiff of defendant's obligation to comply with the statute. Neither text expressly applies to the plaintiff's waiver of his right to sue in a federal court. Moreover, the rule of *Wilko* v. *Swan* does not entirely prohibit the plaintiff's waiver of that right; the case merely decided *when* plaintiff may not waive a right—namely, before the dispute under the 1933 Act has arisen.[11] Thus, I do not read *Wilko* v. *Swan* as a case giving fixed meaning to ambiguous statutory language. Rather, I believe it is more fairly construed as a case holding that in certain situations the enforceability of arbitration agreements should be denied as contrary to the public policy expressed in the statute as a whole, and extending the literal coverage of § 14 of the Act to achieve that purpose.[12]

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[10] In the court of appeals the issue in *Wilko* v. *Swan* was stated as "whether the 1933 Act evidences a public policy which forbids referring the controversy to arbitration." 201 F.2d at 443. That court accurately pointed out that the question was not expressly answered by the statutory language: "Although the question is not free from doubt and Judge Goddard's opinion presents a strong argument against the conclusion we have reached, we do not find in the purpose or in the language of the statute, any policy argument strong enough to override the policy of the Arbitration Act. If Congress had intended to forbid arbitration in a suit based on section 12(2), we believe it would have expressed such intent." *Id.* at 445.

[11] See *Coenen* v. *R. W. Pressprich & Co.*, 453 F.2d 1209, 1213 (2d Cir. 1972).

[12] In the Summary of Argument in its brief Amicus Curiae in the Supreme Court, the Securities and Exchange Commission relied primarily on statutory policy rather than statutory language: "The arbitration provision should be held invalid because of conflict with the policy of Congress, and as an attempted waiver of the customer's

(footnote continued)

The same rationale justifies an expansion of the coverage of § 29(a) of the 1934 Act beyond its literal meaning to find unenforceability of arbitration agreements which would defeat the purposes of that Act.[13] But in a case such

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statutory rights prohibited by Section 14 of the Act." Amicus Brief, p. 11. Its public policy argument was also advanced independently of § 14: "Wholly apart from the inclusion of an express anti-waiver provision in a statute, public policy prohibits the recognition and enforcement of stipulations limiting or preventing access to the courts where the statutory rights involved, although conferred on a private party, are affected with a public interest." *Id.* at 23.

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[13] See *Reader* v. *Hirsch & Co.*, 197 F.Supp. 111 (S.D.N.Y. 1961), holding that a broker could not compel a customer to arbitrate a claim for losses allegedly resulting from a violation of the margin requirement of § 7 of the 1934 Act.

It is interesting to note that in *Axelrod & Co.* v. *Kordich, Victor & Neufeld*, 451 F.2d 838 (2d Cir. 1971), after demonstrating that § 28(b) of the 1934 Act made it perfectly clear that § 29(a) did not preclude enforcement of the compulsory arbitration rules of the New York Stock Exchange, Judge Timbers, who had presented the oral argument on behalf of the S.E.C. in *Wilko* v. *Swan*, see 346 U.S. at 427-428, thought it appropriate to add this dictum:

> "Moreover, the policy considerations relied on by the Supreme Court in *Wilko* are inapposite here. The Supreme Court found that the non-waiver provision there involved was designed to protect investors. 346 U.S. at 431. Without such provision, financial houses might escape statutory liability by taking advantage of the inferior bargaining position of customers. But the legislative policy of protecting investors will not be thwarted by compelling an exchange member to arbitrate, at the instance of a nonmember, a dispute which is arbitrable under the exchange's constitution." *Id.* at 842-843.

My appraisal of this case is not supported by a provision comparable to § 28(b), but I consider it plain that the policy of the 1934 Act would not be thwarted by enforcing this agreement, whereas the strong countervailing policy identified by the Chief Justice in *Zapata* will be compromised if it is not enforced.

as this, and no doubt in less extreme cases as well, I would interpret § 29(a) as meaning no more than it actually says, and respect what I regard as the stronger policy mandated by § 201 of the Federal Arbitration Act, 9 U.S.C. § 201.

The dispute between these parties over the alleged shortage in defendant's inventory of European trademarks, a matter covered by contract warranties and subject to preclosing verification, is the kind of commercial dispute for which arbitration is entirely appropriate. In my opinion, the fact that the "fraud" language of Rule 10(b)(5) has been included in the complaint is far less significant than the desirability of having the Court of Arbitration of the International Chamber of Commerce in Paris, France, decide the various questions of foreign law which should determine the rights of these parties. I would require this representative of the American business community to honor its bargain.

I respectfully dissent.

APPENDIX B

IN THE

UNITED STATES DISTRICT COURT
for the Northern District of Illinois, Eastern Division

ALBERTO-CULVER COMPANY,
a Delaware corporation,

Plaintiff

vs.

FRITZ SCHERK,

Defendant.

No. 71 C 1414

MEMORANDUM OF DECISION

January 17, 1972

This cause is before this Court on defendant Scherk's motion to dismiss this action on a number of grounds: lack of subject matter jurisdiction, lack of personal jurisdiction over Scherk, and on the basis of the doctrine of forum non conveniens. In the alternative defendant moves to stay these proceedings pending arbitration before the International Chamber of Commerce. Finally, defendant moves to strike the claim for exemplary damages contained in Counts I and III.

SUMMARY OF FACTS

The plaintiff, Alberto-Culver (hereinafter referred to as "Alberto") is a Delaware corporation whose principal place of business is located in Melrose Park, Illinois. It is engaged in the business of manufacturing and marketing cosmetic products for domestic and international markets.

Defendant Scherk is a German citizen who presently resides in Geneva Switzerland. Prior to the instant dispute

Scherk owned several businesses which were engaged in the manufacture and distribution of cosmetic products in Western Europe and various other international markets. The sale to Alberto of three of these businesses is the subject matter of this law suit. *Scherk Establissement Vaduz* (hereinafter referred to as "SEV"), was originally a Liechtenstein business entity which was subsequently transformed at the request of Alberto into a Liechtenstein corporation. SEV was a corporate holding company which licensed the international distribution of various Scherk products under a variety of trademarks which were held by SEV. Pursuant to the contract Alberto acquired all of the SEV stock.

The second business acquired by Alberto was a German corporation, *Lodeva Herstellung und Vertrieb Kosmetischer Artikel* GMBH (hereinafter referred to as "Lodeva"). The third business purchased by Alberto was a sole proprietorship known as *Firma Ludwig Scherk* (hereinafter referred to as "FLS").

After preliminary contacts between the two parties in June and November of 1967 serious negotiations for the purchase of the three businesses began in December 1967, when Mr. Lavin, the President of Alberto, and Benjamin Navon, defendant's brother-in-law and plant manager, met in Melrose Park, Illinois to discuss the nature and background of FLS, SEV and Lodeva. At this meeting the discussion primarily focused on acquisition of FLS rather than the acquisition of SEV or Lodeva.

In February, 1968, Alberto contacted Scherk in a successful effort to resume negotiations. A series of discussions between Lavin and Scherk in Berlin culminated in a 3-day meeting in late May and early June of 1968 in Melrose Park, Illinois. Representing the Scherk interests were Messrs. Scherk and Navon and Mr. Stuart Marks. Mr.

Lavin and several other executives represented Alberto Culver. At that meeting agreement was reached as to the basic provisions of the sale of FLS, SEV and Lodeva to Alberto.

After the May-June, 1968 meeting ancillary negotiations took place in both Europe and the United States between the representatives of each side in order to produce a written agreement satisfactory to both parties. In February 1969, Scherk signed the various agreements in Vienna, Austria. (See Complaint, Par. 4). The closing took place in Geneva, Switzerland in June 1969.

The three-count Complaint filed by plaintiff, Alberto, alleges that defendant Scherk made false and fraudulent misrepresentations and omissions as to material facts in connection with plaintiff's purchase from defendant of the three business entities. The gist of plaintiff's complaint is that defendant misrepresented the value and validity of certain trademarks held by SEV which were an integral component of the transaction in question.

Count I alleges a violation of Section 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5 promulgated thereunder. Count II alleges a violation of common law liability for fraud and deceit and for breach of expressed contractual warranties. Count III seeks alternative relief and stands or falls on the validity of Counts I and II. Counts I and II seek as relief recision of the contract between Alberto and Scherk, compensatory damages, exemplary damages, costs, and an injunction forbidding arbitration of the dispute pursuant to the sales contract.

Defendant, Fritz Scherk, has moved to dismiss the Complaint in the above captioned case on several grounds: (1) That the Complaint fails to state a cause of action

under Section 10(b) and Rule 10b-5 of the 1934 Securities Exchange Act, as amended, 15 U.S.C. Section 78j; (2) That the activities complained of were extra-territorial and Section 10(b) does not regulate extra-territorial conduct; (3) That the Court does not have *in personam* jurisdiction over the defendant Fritz Scherk; and, (4) That the action should be dismissed on the basis of the doctrine of *forum non conveniens*. In the alternative, the defendant moves that the proceedings in this Court be stayed pending the outcome of arbitration proceedings in Paris, France before the Court of Arbitration of International Chamber of Commerce. Finally, defendant has moved that the claim for exemplary damages contained in Counts I and III of the Complaint be stricken.

For the reasons set out below defendant's motion to dismiss is denied. The Court finds that the Complaint states a cause of action under Section 10(b) of the Securities Exchange Act of 1934, and Rule 10b-5 promulgated thereunder. The Court further finds that the service of process on defendant Scherk was properly effected and that the "minimal contacts" requirement of the 14th Amendment due process clause of the United States Constitution has been satisfied. Therefore, the Court has jurisdiction over both the subject matter and the defendant Scherk. The Court also finds that the doctrine of *forum non conveniens* is inapplicable to the instant action. In addition, defendant's motion to stay these proceedings pending the pursuit of arbitral remedies before the International Chamber of Commerce is denied. Finally, defendant's motion to strike the claim for exemplary damages in Counts I and III is granted, and it is hereby ordered that Par. 4 of the Prayer for Relief in Count I and Par. 3 of the Prayer for Relief in Count III be stricken.

SUBJECT MATTER JURISDICTION

The defendant's contention that this Court lacks subject matter jurisdiction rests upon two distinct grounds: First, that the conduct complained of fails to state a cause of action under Section 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5; and, secondly, that the conduct which is the subject of the instant complaint occurred outside the United States and is not subject to United States legislative regulation.

Scherk contends that plaintiff's action fails to state a cause of action under Section 10(b) and Rule 10b-5 because there were no "securities" involved in the transaction, and, further, none of the "alleged fraudulent representations applied to [the securities]".

Scherk's first contention is clearly inaccurate. In regard to the acquisition of FLS, it is clear from the affidavits submitted to this Court that Alberto purchased (with certain exceptions) all of the assets of FLS. The acquisition of Lodeva was a transfer of the securities of a German corporation. (See Complaint, Par. 3; Brief in Support of Defendant's Motion to Dismiss or Alternatively to Stay, p. 8). The mere fact that the written agreement fails to refer to "securities" does not negate the fact that securities were in fact transferred. Finally, the purchase agreement (Complaint Exhibit 1, Sec. 1.1) provides that Alberto would have an irrevokable option (which was exercised) to purchase:

> "All issued and outstanding shares of stock of a new Liechtenstein corporation (hereinafter called 'AG' to be formed by seller in accordance with Section 1.4. AG shall own all assets . . . of Scherk Establissment Vaduz, a Liechtenstein establishment (hereinafter called "SEV"), as of the date of the transformation described in Section 1.4." Complaint, Exhibit 1, §1.1

The fact that SEV was converted into a corporation at the behest of Alberto is irrelevant and fails to support defendant's contention that securities were not involved in the transfer.

As the above language demonstrates the parties contemplated and effected a transformation of SEV from a sole proprietorship to a "stock corporation."

The three acquisitions involve the transfer of "securities" as defined by Section 3(a)(10) of the Securities Exchange Act of 1934, as amended, 15 U.S.C. Section 78c (a) (10).

Scherk's contention that the allegedly false representations did not apply to the securities but rather applied to the trademarks is not well taken. Alberto's primary interest in acquiring the trademarks is well documented by the affidavits and pleadings spread of record before this Court. If false representations or omissions were made as to the value of the trademarks, then the false representations were made "in connection with the purchase . . . of any security." For Section 10(b) and Rule 10b-5 clearly cover the situation where, as here, the alleged fraud relates to the value underlying the securities rather than to the securities *per se*. See *Kohler* v. *Kohler*, 319 F. 2d. 634 (7th Cir. 1963).

The value and validity of the trademarks, particularly in this transaction, determined the value of the securities to Alberto.

> "Section 10(b) must be read flexibly, not technically or restrictively. Since there was a 'sale' of a security and since fraud was used 'in connection with' it, there is regress under Section 10(b)."

Superintendent of Insurance, as liquidator of *Manhattan Casualty Company* v. *Bankers Life and Casu-*

alty Company, United States Supreme Court, No. 70-60 November 8, 1971, slip opinion, page 6.

It is found then that the alleged fraudulent misrepresentations and omissions were made "in connection with the purchase" of the above securities. Therefore, the Complaint states a cause of action under Section 10(b) and Rule 10b-5.

Having found that a cause of action is stated under Section 10(b) and Rule 10b-5, the Court must now focus its attention on the issue of whether or not any of the alleged violations of the Rule occurred within the boundaries of this District.

The basic theory propounded by the defendant to support its contention is that Section 10(b) does not regulate "foreign" transactions; that the elements of the transaction are basically "foreign"; and, therefore, the instant case is not subject to Section 10(b) regulation.

The Court is of the opinion that, although much of this complex and prolonged transaction occurred extra-territorially there was sufficient contact within the territorial boundaries of the United States to subject the transaction to the jurisdiction of this Court.

The facts that lead to this conclusion are numerous. First, the crucial negotiations which led to the consummation of the transaction were held in Melrose Park, Illinois in May-June 1968. It was at this three-day meeting between Scherk and Lavin that the basic agreement to acquire the Scherk businesses was reached. This finding is supported by a letter dated June 6, 1969 addressed to Lavin from the defendant Scherk in which the defendant states:

"It is more than a year ago that we last met at Melrose Park to agree upon a transaction which will now

at long last come to its closing . . . I, therefore, invite you to come to Geneva at a date convenient to everyone in order to close the deal which I was glad to agree to at your office one year ago." Lavin Affidavit, Exhibit B.

It has not been conclusively demonstrated that Mr. Scherk made any "untrue statement of material fact." However, the sanctions of Rule 10b-5 are not limited to positive fraudulent misrepresentation, but, in addition, forbid failure "to state a material fact necessary in order to make the statement made, in the light of the circumstances under which they were made, not misleading." (Rule 10b-5 (2), 17 CFR 240-10b-5). If the defendant failed to advise plaintiffs of the actual value of the trademarks held by the defendant while aware of the value that the plaintiffs attached to the trademark, then defendant would have failed to state a material fact, the omission of which, in light of the surrounding circumstances, would have been misleading. Such allegations, if accurate, would indicate that a serious violation of Rule 10b-5 had occurred within the Northern District of Illinois.

Secondly, the communications between Alberto and Mr. Marks, defendant's attorney, subsequent to the May-June 1968 meeting, as to the validity, value and non-contested status of the trademarks in contention occurred within the territorial jurisdiction of the United States. (See Silver affidavit. Exhibits A through L).

Finally, the full economic impact of the alleged fraud occurred within the United States. Alberto is a Delaware corporation whose principal place of business is located in Illinois. Its securities are traded on the New York Stock Exchange. The economic impact caused by the alleged misrepresentation and omissions was absorbed by Alberto-Culver.

For these reasons, the cases cited by defendant in support of its position are inapposite. In *Finch* v. *Marathon Securities Corporation,* 316 F. Supp. 1345 (S.D.N.Y. 1970), the District Court held that it lacked subject matter jurisdiction over a 10b-5 action brought by a British resident against other foreigners for injuries sustained as a result of being fraudulently induced in England to buy securities of a foreign corporation. There was no allegation of domestic injury or consequence. In so holding, the District Court noted that

> "when, as here: (1) the substance of the allegedly fraudulent conduct occurred outside the United States; (2) the parties are predominantly foreign; (3) the subject shares are securities in a foreign corporation, neither registered nor traded on a national exchange; and (4) there is no showing of any domestic injury, it would appear that the District Court is without subject matter jurisdiction, despite the existence of other less meaningful American based facts and events." 316 F. Supp. at 1349.

The *Finch* case is not persuasive precedent for the instant fact situation. In the suit before this Court the substance of the allegedly fraudulent activity occurred within the United States. The parties here are not "predominantly foreign". Finally, there has been a showing of domestic injury as a result of the alleged fraudulent activity.

This Court will follow the careful and well-reasoned opinion of Judge Levet in *Ferraioli* v. *Cantor,* 259 F. Supp. 842 (S.D.N.Y. 1966). In that case, a former shareholder filed suit under Section 10(b) and Rule 10b-5 against a Canadian corporation which held controlling interest in a New York corporation for transferring control of the New York corporation at a premium while failing to disclose the premium offered and affording equal opportunity for other shareholders to participate in

the transaction. The District Court held that it had jurisdiction over the subject matter of the law suit. The Court stated:

> "All in all, it is my opinion that the course of conduct which is alleged as a violation of the Securities Exchange Act of 1934 in this case occurred at least in part within the United States and that jurisdiction of the United States Courts over the subject matter of this action is sustained by those acts." 259 F. Supp. 842, 846.

Accordingly, this Court holds that it has jurisdiction of the subject matter of this suit. The Complaint states a cause of action under Section 10(b) and Rule 10b-5. Further, a portion of the alleged fraudulent activity occurred within the jurisdiction of this District.

PERSONAL JURISDICTION

The second prong of defendant's motion to dismiss is based on the contention that this Court lacks personal jurisdiction over the defendant Scherk because (1) service of process was ineffective and should therefore be quashed, and, in the alternative (2) that the 14th Amendment due process requirement of "minimal contacts" has not been satisfied by Scherk's limited connection with the United States.

Although initial service of process may have been faulty, Scherk was served by Swiss authorities on October 8, 1971 with copies of the Summons and Complaint in accordance with Rule 4(e) and 4(i), Fed. R. Civ.P. and Swiss law. The issue of whether service of process was properly effected is now moot. Under Section 27 of the Securities Exchange Act of 1934, "process . . . may be served . . . wherever the defendant may be found." The combination of Section 27, when read in conjunction with Rules 4(e) and 4(i) permits service in a foreign

country. *SEC* v. *VTR, Inc.*, 39 F.R.D. 19 (S.D.N.Y. 1966); *Ferraioli* v. *Cantor*, 259 F. Supp. 842 (S.D.N.Y. 1966).

The remaining substantive issue is whether the 14th Amendment due process requirement of "minimal contacts" precludes this Court from assuming personal jurisdiction over the defendant Scherk. Cf. *International Shoe Company* v. *State of Washington*, 326 U.S. 310 (1945); *McGee* v. *International Life Insurance Company*, 355 U.S. 220 (1957).

Scherk's visit to Melrose Park, Illinois in May-June 1968 and his attorney's visit to Chicago on December 8, 1968 satisfies the minimal contact requirement of the 14th Amendment due process clause. (See Exhibits A through L of Silver Affidavit) *International Shoe Company* v. *Washington, supra.* The "minimal contact" concept found in *International Shoe* has been extended in *McGee* v. *International Life Insurance Company, supra,* where the United States Supreme Court held that even a single act by an out of state corporation may subject it to the jurisdiction of the forum state if the cause of action in question arises out of that act. See *Livingston* v. *Weiss, Voison, Cannon, Inc.*, 294 F. Supp. 676, 682-683 (D.N.J. 1968). Thus, it has become a firmly established rule that personal jurisdiction over the defendant will be sustained if the defendant was properly served and has committed even a single act within the forum which is a substantial and material part of the violation. *Hooper* v. *Mountain State Securities*, 282 F. 2d. 195 (5th Cir. 1960), cert. den. 395 U.S. 814 (1968); *Clapp* v. *Stearns*, 229 F. Supp. 305, 307 (S.D.N.Y. 1964).

This Court concludes that the alleged fraudulent conduct of defendant and defendant's agent is sufficient to satisfy the 14th Amendment due process requirements of "minimal contacts". Therefore, the service of process

having been properly effected, this Court has personal jurisdiction over the defendant Scherk.

FORUM NON CONVENIENS

Forum Non Conveniens is a doctrine which permits a court to dismiss an action although jurisdiction is validly asserted when in the court's discretion convenience of the parties and the ends of justice would be better served if the action were entertained in another forum.

Title 28 U.S.C. §1404(a), enacted in 1948, codified and replaced the doctrine of *forum non conveniens* in situations where the more convenient tribunal is a United States District Court where the action could originally have been filed. See *Norwood* v. *Kirkpatrick*, 349 U.S. 29 (1955).

However, the doctrine has retained its original vitality as to cases which lie outside the scope of §1404(a). For example, a Federal Court possesses the inherent power to refuse to exercise its jurisdiction over a case which may have been originally instituted before a foreign tribunal. *DeSainigne* v. *Gould*, 177 F. 2d. 515 (2nd Cir. 1947); *Vanity Fair Mills* v. *T. Eaton Co.*, 234 F. 2d. 633 (2nd Cir. 1956). *cert. den.* 352 U.S. 871. Thus, the instant case is governed by the doctrine of *forum non conveniens* rather than the provisions of 28 U.S.C. §1404(a).

It should be noted that the power to refuse to exercise jurisdiction when it has been validly asserted lies within the discretion of the trial judge. The doctrine is a harsh rule and should be invoked and applied only in rare and exceptional cases. *Glicken* v. *Bradford*, 204 F. Supp. 300 (D.C.N.Y. 1962).

Defendant's motion to dismiss on the basis of *forum non conveniens* is denied. It has been repeatedly held that doctrine is inapplicable to causes of action brought under

a statute which specially provides for venue. *Baltimore & Ohio Railroad* v. *Kemper*, 314 U.S. 44 (1941) (F.E.L.A.); *United States* v. *National City Lines*, 334 U.S. 573 (1948) (Clayton-Anti-Trust Act). While defendant notes that neither case deals with the Securities Exchange Act, his conclusion that the cases are inapposite is in error. In *Gulf Oil Corporation* v. *Gilbert*, 330 U.S. 501 (1947) the United States Supreme Court, after noting that in *Kemper* that plaintiff's choice of forum under the F.E.L.A. could not be defeated by the doctrine of *forum non conveniens* because of the special venue section of the statute stated that "those decisions do not purport to modify the doctrine as to other cases governed by the *general* venue statutes." 330 U.S. at 505. (Emphasis added)

Further, in its opinion, the Court stated:

> "the principle of forum non conveniens is simply that a Court may resist imposition on its jurisdiction even when jurisdiction is authorized by the letter of the *general* venue statute. These statutes are drawn with a necessary generality and usually give a plaintiff a choice of court, so that he may be sure of some place in which to pursue his remedy." 330 U.S. at 507.

Finally, the holding of the United States Supreme Court that the special venue provisions of the F.E.L.A. and the Clayton Act were subject to §1404(a) is inapposite here. See *Ex Parte Collett*, 337 U.S. 55 (1949); *Kilpatrick* v. *Texas & Pacific R. R.*, 337 U.S. 75 (1949); *United States* v. *National City Lines*, 337 U.S. 78 (1949). As was noted above, the doctrine of *forum non conveniens* rather than §1404(a) governs the disposition of defendant's motion. Thus, a ruling that §1404(a) is applicable to statutes containing a special venue provision does not dictate or even imply that *forum non conveniens* has lost its vitality.

Both *forum non conveniens* and §1404(a) proceed on the assumption that there is an alternative tribunal which will be more hospitable to plaintiff's claim. *Odita* v. *Elder Dempster Lines, Ltd.*, 286 F. Supp. 557, (S.D.N.Y. 1968.) *Silver* v. *Country Wide Realty, Inc.*, 39 F.R.D. 596 (D.C. N.Y. 1966). United States Courts have exclusive jurisdiction of actions under the Securities Exchange Act of 1934. Securities & Exchange Act, Section 27, 15 U.S.C. §78aa. Although the International Chamber of Commerce arbitration court is available for pursuit by plaintiff of his contractual remedies it is not available to try the cause of action alleged under Section 10(b) and Rule 10b-5. The net result is that there is no District Court to which the action could be transferred pursuant to §1404 (a), nor is there an alternate tribunal which plaintiff could utilize if he were to be dismissed from this Court in accord with the doctrine of *forum non conveniens* in which he could pursue his remedies under Section 10(b) and Rule 10b-5. For the above reasons defendant's motion to dismiss on the basis of *forum non conveniens* is denied.

STAY OF PROCEEDINGS

Assuming that this action is not dismissed for any of the foregoing reasons, defendant has moved in the alternative to stay the proceedings before this Court in order to allow the parties to pursue their contractual remedies before the International Chamber of Commerce tribunal in Paris, France.

In *Wilco* v. *Swan, et al.*, 346 U.S. 427 (1953) the United States Supreme Court held that an agreement to arbitrate future controversies relating to a margin purchase agreement which was entered into by a securities broker and a purchaser was voided by Section 14 of the Securi-

ties Exchange Act of 1933, as amended, 15 U.S.C. Sec. 77n. The issue before the Court was

> "whether an agreement to arbitrate a future controversy is a 'condition, stipulation, or provision binding on any person acquiring any security to waive compliance with any provision of the Securities Act which Section 14 declares 'void' " 346 U.S. at 430.

The Court characterized the arbitration clause contained in the contract as a "stipulation", and concluded that "the right to select the judicial forum is the kind of 'provision' that cannot be waived under Section 14 of the Securities Act." 346 U.S. at 435.

The Court stated that "we decide that the intention of Congress concerning the sale of securities is better carried out by holding invalid such an agreement for arbitration of issues arising under the Act." 346 U.S. at 438.

Defendant seeks to avoid the thrust of the *Wilco* decision by limiting the application of that case to arbitration agreements executed prior to the existence of any controversy. Defendant correctly contends that *Wilco* is inapplicable to an arbitration agreement entered into in order to settle an existing dispute. This is an accurate statement of the case. However, defendant's attempt to characterize the contractual agreement to arbitrate as an election by the plaintiff "to submit an existing dispute to arbitration" must fail.

The federal cause of action in this case is based upon Section 10(b) and Rule 10b-5 of the Securities & Exchange Act of 1934. The United States District Courts have exclusive jurisdiction of this type of law suit. (See page 18) Therefore, the defense raised by SEV in the Liechtenstein court that defendant's (plaintiff in the Liechtenstein action) claim was subject to arbitration

does not constitute an agreement by *both* parties to submit an existing Section 10(b) dispute to arbitral jurisdiction.

Therefore, defendant's motion to stay these proceedings pending arbitration before the International Chamber of Commerce is denied.

EXEMPLARY DAMAGES

Defendant's motion to strike the prayer for exemplary damages based upon violations of Section 10(b) and Rule 10b-5 is granted. Plaintiff's request for relief contravenes the explicit statutory language contained in Section 28(a) of the Act which provides that ". . . [N]o person permitted to maintain a suit for damages under the provisions of this chapter shall recover . . . a total amount in excess of his actual damages on account of the act complained of." Section 28(a) Securities Exchange Act of 1934, as amended, 15 U.S.C. Section 78 bb (a)."

Although this specific issue has not been decided by the Seventh Circuit Court of Appeals, the interpretation of Section 28 (a) which precludes the recovery of punitive damages in a private suit under Section 10(b) has been repeatedly upheld. *Green* v. *Wolf Corp.*, 406 F. 2d. 291 (2nd Cir. 1968) *cert. den.* 395 U.S. 977 (1969); *Globus* v. *Law Research Service, Inc.*, 418 F. 2d. 1276 (2nd Cir. 1969) *cert. den.* 397 U.S. 913 (1970).

Therefore, it is hereby ordered that Par. 4 of the Prayer for Relief in Count I and Par. 3 of the Prayer for Relief in Count III be stricken from the Complaint.

/s/ William J. Lynch
Judge, United States District Court

Dated: January 17, 1972

APPENDIX C

In the

United States Court of Appeals

For the Seventh Circuit

August 2, 1973

No. 72-1158

ALBERTO-CULVER COMPANY, a Delaware Corporation,

Plaintiff-Appellee,

vs.

FRITZ SCHERK,

Defendant-Appellant.

Appeal from the United States District Court for the Northern District of Illinois, Eastern Division.

This cause came on to be heard on the transcript of the record from the United States District Court for the Northern District of Illinois, Eastern Division, and was argued by counsel.

On consideration whereof, it is ordered and adjudged by this court that the judgment of the said District Court in this cause appealed from be, and the same is hereby, AFFIRMED, with costs, in accordance with the opinion of this Court filed this day.

(SEAL)

APPENDIX D

In the

United States Court of Appeals

For the Seventh Circuit

October 18, 1973.

No. 72-1158

ALBERTO-CULVER COMPANY,

Plaintiff-Appellee,

vs.

FRITZ SCHERK,

Defendant-Appellant.

Appeal from the United States District Court for the Northern District of Illinois, Eastern Division.

On consideration of the petition for rehearing and suggestion that it be heard *en banc* filed in the above-entitled cause, no judge in active service having requested a vote thereon, nor any judge voted to grant the suggestion, and all of the members of the panel having voted to deny a rehearing,

IT IS ORDERED that the petition for a rehearing in the above-entitled cause be and the same is hereby denied.

APPENDIX E

The Federal Arbitration Act, 9 U.S.C.

Section 2.

A written provision in any maritime transaction or a contract evidencing a transaction involving commerce to settle by arbitration a controversy thereafter arising out of such contract or transaction, or the refusal to perform the whole or any part thereof, or an agreement in writing to submit to arbitration an existing controversy arising out of such a contract, transaction, or refusal, shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract.

Section 3.

If any suit or proceeding be brought in any of the courts of the United States upon any issue referable to arbitration under an agreement in writing for such arbitration, the court in which such suit is pending, upon being satisfied that the issue involved in such suit or proceeding is referable to arbitration under such an agreement, shall on application of one of the parties stay the trial of the action until such arbitration has been had in accordance with the terms of the agreement, providing the applicant for the stay is not in default in proceeding with such arbitration.

Section 201.

The Convention on the Recognition and Enforcement of Foreign Arbitral Awards of June 10, 1958, shall be enforced in United States courts in accordance with this chapter.

Section 202.

An arbitration agreement or arbitral award arising out of a legal relationship, whether contractual or not, which is considered as commercial, including a transaction, contract, or agreement described in section 2 of this title, falls under the Convention. An agreement or award arising out of such a relationship which is entirely between citizens of the United States shall be deemed not to fall under the Convention unless that relationship involves property located abroad, envisages performance or enforcement abroad, or has some other reasonable relation with one or more foreign states. For the purpose of this section a corporation is a citizen of the United States if it is incorporated or has its principal place of business in the United States.

Section 206.

A court having jurisdiction under this chapter may direct that arbitration be held in accordance with the agreement at any place therein provided for, whether that place is within or without the United States. Such court may also appoint arbitrators in accordance with the provisions of the agreement.

Section 208.

Chapter 1 applies to actions and proceedings brought under this chapter to the extent that chapter is not in conflict with this chapter or the Convention as ratified by the United States.

Securities Act of 1933, Section 14

Any condition, stipulation, or provision binding any person acquiring any security to waive compliance with any provision of this subchapter or of the rules and regulations of the Commission shall be void.

Securities Exchange Act of 1934, Section 29(a)

Any condition, stipulation or provision binding any person to waive compliance with any provision of this chapter or of any rule or regulation thereunder, or of any rule of an exchange required thereby shall be void.